International Securities and Capital Markets—Developments in 2005

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I. Developments in Brazil

A. New Listing Segment in the Organized Over-the-counter Market

On May 16, 2005, BOVESPA, the São Paulo Stock Exchange, introduced the BOVESPA MAIS (MAIS), a segment of the organized over-the-counter market, regulated by Instruction CVM No. 243, of March 1, 1996, and run by BOVESPA, and to which only public companies registered with the Brazilian Securities and Exchange Commission will have access. MAIS is intended to provide companies a gradual access strategy to the capital markets, facilitate visibility in the market, and support companies' efforts in transparency, shareholder diversification, and liquidity. A MAIS listing could provide an avenue for several different strategies of market access, such as small-scale IPOs, including those followed by a broader offering, or listings without an accompanying offering carried out for visibility purposes.

In order to participate in MAIS, a company must provide greater rights to shareholders and disclose more information than would be required in the New Market (*Novo Mercado*). A company must also work to construct a solid and net market for its publicly disclosed documents, demonstrating a disposition to reach higher levels of transparency in the capital markets. The following are the main characteristics of MAIS:

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(i) Trading takes place on the Mega Bolsa's electronic platform. Investment banks, securities brokers, and dealers can participate.

(ii) To qualify for listing on MAIS, a company must issue only common shares (existing preferred shares may not be listed); ensure all existing holders of common shares a tag-along right on the same terms as those offered by the selling controlling shareholder in sales of a controlling stake; offer their shares publicly for their firm value if the company goes private or withdraws from MAIS; agree to submit to the Market's Arbitration Chamber to settle any corporate disputes; have a Board of Directors whose members will not hold office for longer than two years; provide additional information on the ITR (quarterly information), DFP (standardized financial statements) and IAN (annual information) reports, such as cash flow, quarterly consolidated statements, equity positions of administrators and controllers, controlling shareholder transactions, and the annual corporate events calendar.

(iii) To maintain its listing on MAIS, a company must show a minimum free float of 25 percent within up to seven years of the date of listing. If the company fails to reach the minimum free float, it may be allowed to continue on the MAIS if it has had a minimum of ten trades a month and a minimum 25 percent presence in trading sessions at the end of each fiscal year. Additionally, the company will be delisted if it has five consecutive years of loss combined with a negative net worth in the previous three years, or a negative net worth for five consecutive years combined with losses in the immediately preceding years.

(iv) BOVESPA offers support to listed companies, including: guidance on the process of going public, current laws and regulations, and MAIS rules; training courses regarding relationships with investors and corporate governance; preparation of regular analysis reports of listed companies to be published to the market; publication of the profiles of the listed companies; and the maintenance of a page, on the BOVESPA website, dedicated to the segment and to MAIS companies.

B. The SPC in the Brazilian Public-Private Partnership Program

Another new development that may have a favorable impact on the development of the Brazilian capital market is the mandatory use of a Specific Purpose Company (SPC) in connection with so-called Public-Private Partnerships (PPPs). Law 11079, of December 30, 2004,[1] lays down the general guidelines to bid and contract under the PPP modality.[2] PPPs are contracts of concession that may be sponsored or administrative. A sponsored contract relates to concessions given out for public utilities or works and involves not only the tariffs collectable from users, but also the pecuniary consideration of the public partner towards the private partner. Administrative services contracts are those wherein the Administration is the direct or indirect user of the services.

1. The purpose of this law is to render possible private investments in infrastructure projects such as city development, basic sanitation, energy, gas, roads, irrigation and drainage systems, ports, and transportation in general.

2. In Brazil, the public party in those partnerships are all the instrumentalities, special funds, departments (*autarquias*), public foundations, public companies (*empresas públicas*), public-private companies (*sociedades de economia mista*), and other companies controlled by the federal, state, or local governments, whether directly or indirectly. The private party is, therefore, all other entities performing in the private sector.

According to the new legislation, an SPC must be organized prior to the execution of the contract to implement and manage the partnership. The transfer of control from the SPC is conditioned on the express authorization of the public partner, as defined in the public notice of invitation to bid and contract. In order to secure such authorization, the candidate must undertake to satisfy all the conditions contained in the contract in force. SPCs may be publicly held companies whose securities are listed for trading on a stock exchange and who meet certain corporate governance requirements and use standardized accounting practices as per the regulation. The public partner must not hold the majority of the voting capital in the SPC. This prohibition, however, does not apply to the acquisition of majority ownership in the SPC's voting capital by a financial institution controlled by a state-owned entity in the event of default under financial agreements, insofar as such institution acts as the PPP financier.

Additionally, the PPP contracts may contain provisions relating to: (i) the requirements and conditions for the state-owned entity to authorize the transfer of control in the SPC to its financiers, with a view to promoting its financial reestablishment and ensuring that services will continue to be provided; (ii) the possible issuance of pledges in the names of those funding the project with respect to the pecuniary obligations of the public partner; and (iii) the eligibility of project financiers to receive indemnification for early termination of the contract or default on payments made by funds and state-owned companies guaranteeing the PPPs.

PPPs may become a strong ally of the government in attracting new foreign investment to Brazil. If the SPCs created in the implementation of such projects are organized as publicly held companies, this modality may help improve and strengthen the Brazilian capital market.

II. Developments in Canada

A. Introduction

Developments in Canada in the securities area continue to mirror many of the developments in the rest of the world, with Canada attempting to come to grips with how to achieve efficient and fair markets without imposing unnecessary costs on market participants. The discussion that follows focuses on the key developments in 2005.

B. Civil Liability for Disclosure in the Secondary Market

The most significant change in Canadian securities legislation in 2005 has been amendments to the Ontario Securities Act that impose civil liability for misrepresentations in the secondary market.[3] Until these amendments were made, securities legislation in each of the provinces of Canada only imposed civil liability for misrepresentations in prospectuses or take-over bid circulars in the primary market. This was the case notwithstanding that secondary market trading accounted for most of the trading in Canadian capital markets.

Under the amendments, investors now have the right to sue for a misrepresentation in a filed document or a public oral statement and for a failure to make timely disclosure of a

3. Ontario Securities Act, S.O., ch. 22 (2002), amended by 2004 S.O., ch. 31 (Can.).

material change in the issuer's business. A document is defined to include any written communication, including electronic communications.

The legislation provides that the plaintiff's right of action does not turn on whether the plaintiff relied on the misrepresentation. This removes the most common defense to a civil action at common law for misrepresentation in a secondary market document or statement. The legislation does impose different burdens of proof and liability for different defendants depending on whether the claim is with respect to a document or a failure to make timely disclosure of a material change and, in the case of a document, whether it is a core document (generally those required to be filed at law) or a non-core document.

The legislation provides a number of defenses, including a reasonable investigation defense, a defense for reliance on an expert statement, a defense in the case of non-core documents if the defendant did not know and had no reasonable grounds to believe that a document would be made public, and a defense for a misrepresentation in forward looking information if the document or public oral statement containing the forward looking information contained reasonable cautionary language.

Except in cases where a misrepresentation is made knowingly, liability for an issuer is capped at the greater of 5 percent of its market capitalization or $1,000,000, and in the case of individual defendants, the greater of $25,000 or 50 percent of the aggregate of the individual's compensation from the issuer.

Finally, the legislation attempts to prevent strike suits by requiring leave of the court to commence an action and court approval to settle, discontinue, or dismiss an action for delay. The legislation also provides that a prevailing party is entitled to its costs.

C. Income Trusts

In the last few years, Canadian capital markets have been dominated by income trust offerings. Many businesses with reliable cashflows, but with limited growth potential and modest capital expenditures, have packaged their assets into an income trust, which they then offer to the public. This provides a very favorable valuation of the assets from the vendor's perspective and provides a high-yield, tax-effective, and moderate-risk alternative to fixed-income securities for the investor.

In September 2005, the federal government announced a public consultation process on tax and other issues related to publicly listed flow-through entities.[4] The Minister of Finance also instructed the Canada Revenue Agency not to issue any advance income tax rulings in connection with income trusts.[5] This had the effect of severely curtailing the market, as it was not clear what approach the federal government would adopt with respect to income trusts, with one possibility being the imposition of an income tax upon them. Ultimately, the federal government's solution was to reduce the existing tax on corporate dividends so as to level the playing field between corporations and income trusts.[6] The result of this

4. *See* Press Release, Department of Finance Canada, Department of Finance Launches Consultations on Issues Related to Publicly Listed Flow-Through Entities (Income Trusts and Limited Partnerships) (Sept. 8, 2005), *available at* http://www.fin.gc.ca/news05/05-055e.html.

5. *See* Press Release, Department of Finance Canada, Government Postpones Advance Rulings on Income Trusts and Other Flow-Through Entities: Emphasizes Importance of Consultations (Sept. 19, 2005), *available at* http://www.fin.gc.ca/news05/05-059e.html.

6. *See* Press Release. Department of Finance Canada, Minister of Finance Acts on Income Trust Issue (Nov. 23, 2005), *available at* http://www.fin.gc.ca/news05/05-082e.html.

should be to invigorate the market in income trusts, but at the same time provide issuers taking an entity public with a balanced choice between going the income trust route and using a corporate vehicle. The proposed solution requires an agreement on the part of the provinces to effect a complementary increase in the dividend tax credit, and until the provinces cooperate, the solution is not entirely effective.

D. Hedge Fund Regulation

Also seen in 2005 was the collapse of two large Canadian hedge funds selling principal protected notes to retail clients. Regulatory investigations are ongoing as to the cause of the collapse. The collapse has led to a significant concern on the part of retail investors and has affected sales of hedge fund products. It is estimated that the Canadian hedge fund industry has gone from roughly $4 billion to over $30 billion in the past five years.[7] It is further estimated that hedge funds may actually account for nearly one-third of market activity because of their tremendous trading velocity.[8]

The Chair of the Ontario Securities Commission (OSC) has indicated that the Canadian securities regulators will consider measures designed to ensure that hedge fund managers provide fair, full, accurate, and timely information to their investing clients. In addition, the regulators will consider taking steps to improve transparency regarding fees and risks. As a result of the collapse of the two large hedge funds in 2005, it is quite likely that at a minimum the OSC will propose changes in this largely unregulated area with a view to protecting retail investors.[9]

E. Investment Funds

In 2005, the Canadian securities regulators proposed a rule requiring an independent review committee for investment funds.[10] This rule is part of the Canadian securities regulators' initiatives to improve investment fund governance. The proposed rule imposes a minimum, consistent standard of governance for publicly offered investment funds. Under the proposed rule, every investment fund that is a reporting issuer will have to have a fully independent advisory body called the independent review committee (IRC) to oversee all conflict-of-interest matters faced by a fund manager in the operation of the fund. For any decision by the fund manager that involves or that a reasonable person would assume involves a conflict of interest for the fund manager, the fund manager must establish written policies and procedures that it must follow and refer the matter to the IRC for its review. A decision by the fund manager to engage in certain specified transactions currently restricted by securities legislation must receive the prior approval of the IRC to proceed. For any other proposed course of action by the fund manager that involves, or that a reasonable person would consider involves, a conflict of interest for the fund manager, the IRC must

7. *See* David Wilson, Chairman, Ontario Sec. Comm'n, *Dialogue with the OSC 2005: Setting the Standard* (November 17, 2005), *available at* http://www.osc.gov.on.ca/About/Speeches/sp_20051117_dw_dialogue-opening-remarks.pdf.

8. *Id.*

9. *Id.*

10. Ontario Security Council, *National Instrument 81-107: Independent Review Committee for Investment Funds* (May 27, 2005), http://www.osc.gov.on.ca/Regulation/Rulemaking/Current/Part8/rule_20050527_81-107_supplement.pdf.

provide the fund manager with a recommendation, which the fund manager must consider before proceeding.

F. Reporting in U.S. GAAP

In 2005, the federal government and the province of Ontario enacted amendments to their respective corporate legislation allowing any corporations formed under either the federal business corporations legislation or the Ontario business corporations legislation and registered with the SEC to prepare financial statements in accordance with U.S. GAAP.[11]

G. Securities Enforcement and Other Significant Decisions

There was an emphasis on increased securities enforcement in Canada in 2005. Regulators have increased the number of enforcement staff, and for the first time in recent memory, a non-lawyer has been appointed chair of the OSC with a mandate to increase enforcement resources.

Coupled with that, the regulators have brought enforcement actions against Hollinger. Inc.,[12] which is already the subject of enforcement action in the United States, and secured a conviction for tipping in a very high-profile case involving an employee of an investment dealer. As it is not common to have successful convictions in Canada in the insider trading/ tipping area, this was considered a significant victory for the regulators, even though the individual was sentenced to only six months imprisonment.[13] The OSC is appealing the sentence.

The OSC also issued a decision with significant consequences to the public markets in a proposed going private transaction by the controlling shareholder of Hollinger.[14] The controlling shareholder of Hollinger and certain other insiders were the subject of a cease trade order issued by the OSC because the corporation had not filed financial statements. Hollinger applied for a variation of the cease trade order to allow the going private transaction to proceed. Hollinger's argument was that its minority shareholders should have a right to consider the offer rather than be subject to the significant uncertainties involving all of its litigation and its dysfunction. The OSC exercised its public interest power whereby it can refuse to vary certain orders if it is prejudicial to the public interest and determined that, because of a lack of information provided to minority shareholders, because of the lack of a Board recommendation, and because of other factors surrounding the transaction, it would not vary the cease trade order to allow the transaction to go before shareholders. This was a courageous and, in some circles, unexpected decision on the part of the OSC as it did not allow the transaction to be placed before the shareholders and in effect determined that it would not be in the public interest to allow the transaction to proceed in its current form.

11. Canada Business Corporations Regulations SOR/2001-512 (Can.), amended by SOR/2005-51 (Can.); Business Corporations Act, R.R.O., Reg. 62 (1990), amended by R.R.O., Reg. 246/05, s.6.

12. *See* Press Release, Ontario Securities Commission, OSC Commences Proceedings in Relation to Hollinger Inc., Conrad Black, F. David Radler, John A. Boultbee, and Peter Y. Atkinson (Mar. 18, 2005), *available at* http://www.osc.gov.on.ca/About/NewsReleases/2005/nr_20050318_osc-hollinger-inc.jsp.

13. *See* R. v. Rankin, [2005] O.J. 4871 (July 15, 2005).

14. *See* In the Matter of Certain Directors, Officers and Insiders of Hollinger Inc., [2005] CarswellOnt 1266.

H. Internal Control Rules

In 2004, all of the provinces, except for British Columbia, proposed a rule similar to section 404 of the United States Sarbanes-Oxley Act of 2002.[15] The proposed rule would have: (1) imposed an evaluation of the effectiveness of internal control over financial reporting against a suitable control framework; (2) required maintenance of evidence providing reasonable support for the evaluation of the effectiveness of the internal controls; (3) required the reporting of material weaknesses in internal control over financial reporting; and (4) required an audit of internal control over financial reporting.

The Canadian securities regulators have now determined not to proceed with the rule.[16] Instead, they propose to expand the rule requiring certification of disclosure in an issuer's annual and interim filings to include additional provisions with respect to internal control over financial reporting. Under these additional provisions, the chief executive officer and chief financial officer of a reporting issuer will be required to certify in their annual certificates that they have evaluated the effectiveness of the issuer's internal control over financial reporting as of the end of the financial year and caused the issuer to disclose in its annual MD&A their conclusions about the effectiveness of internal control over financial reporting as of the end of the financial year, based on such evaluation. An issuer will not be required to obtain from its auditor an internal control audit opinion concerning management's assessment of the effectiveness of internal control over financial reporting.

The earliest these new requirements will apply is for financial years ending on or after December 31, 2007.

III. Developments in Japan

A. Disclosure and Insider Violations

In 2004, there were a few serious disclosure violations leading to the delisting of certain companies, including Seibu Railway Co. Ltd. (Seibu), from the Tokyo Stock Exchange (TSE) and other exchanges. In the Seibu case, there was also insider trading by its parent company, Kokudo, which was penalized with a fine of JPY200 million, while Seibu was fined JPY150 million for the disclosure violation. The Seibu case sent shockwaves into the market and led the Financial Services Agency of Japan to announce reforms in order to restore investor confidence, which were followed by proposed rule changes by the TSE.

B. Disclosure Reforms

1. *TSE Rule: Oath as to Timely Disclosure*

In January 2005, TSE introduced new rules, one of which requires the CEO and other representatives of companies listed on the TSE to sign and file an oath in regard to timely disclosure. The form of the oath requires that the company swear that it recognizes the fundamental importance of and undertakes diligently to perform and implement procedures relating to the timely and proper disclosure of company information to the securities mar-

15. Ontario Security Council, *Multilateral Instrument* 52-111 *Reporting on Internal Control over Financial Reporting*, 28 OSCB 1302 (2005).

16. Ontario Security Council, *Reporting on Internal Control Over Financial Reporting*, 29 OSCB 2011 (2006).

ket. A description of the disclosure procedures of the company is required as an attachment. When the company updates or modifies its disclosure procedures, an attachment explaining such update or modification is to be filed.[17]

The filing is made in the name of the company, but the CEO is required to personally sign the document. The first due date for the filing was the end of February 2005, and the oath is required to be updated in five years if the CEO remains in the office. If any successor CEO is appointed, such new CEO will be required to promptly sign and file the oath following his or her assumption of office, replacing the previously filed oath.[18]

2. *TSE Rule: Confirmation of Periodic Disclosure Document*

In addition to the above oaths, the CEO of a TSE listed company is required to confirm that to his or her knowledge, the periodic disclosure documents (annual and semi-annual reports) filed under the Securities and Exchange Law of Japan (SEL) do not contain any false statements as to material facts. This confirmation must be reconfirmed every time a public disclosure document is prepared and filed under the SEL. The TSE rule does not have any specific form for this confirmation, but requires a description of how the CEO has come to such conclusion. This requirement is intended to signify the importance of public disclosure and to ensure that the disclosure is correct in material respects in order to restore investor confidence in the public disclosure.

C. Changes Relating to Disclosure Violation

1. *TSE Rule: Expansion of Grounds for Delisting*

TSE also expanded the possible grounds for delisting a company, with additions such as (1) a material violation of any matter covered by the oath, and (2) any false statements of material fact contained in the disclosure documents filed under the SEL if the TSE determines that it has a material adverse effect.[19]

2. *SEL: Expansion of Administrative Sanction*

In order to expand sanctions for securities law violations, the SEL was amended in 2004 to introduce the administrative sanction called *kachoukin* (surcharge), which came into force as of April 2005. In 2005, further amendments to the SEL were made to cover the violation of continuous disclosure requirements under the SEL. Now such disclosure violations, concerning disclosures both to the primary market and to the secondary market, are penalized with criminal, civil, and administrative sanctions.

3. *Other Disclosure Changes under SEL*

The 2005 SEL changes provide that the current requirement that disclosure documents be provided in the Japanese language only will be relaxed to allow, in some cases, the filing of an English language report. This change will be gradually implemented, initially with the filing of reports on investment funds, effective in December 2005. The timing of the

17. Art 4-4 of the Rule on Timely Disclosure of Corporate Information, Etc. by Issuer of Listed Securities; Sec. 4-2 of Administration of the Rule on Timely Disclosure of Corporate Information, Etc. by Issuer of Listed Securities.

18. *Id.*

19. Art 2, Para 1, Items 11 and 12, of the Standards for Delisting of Stock.

relaxation regarding annual and other securities reports by foreign companies under the SEL has not yet been formally announced, but is expected over the next couple of years.

4. *Further Reforms*

There are a number of other reforms relating to disclosure. Among them are the introduction of a quarterly report under the SEL, together with certification by the CEO and attestation by accountants. Effective in May 2005, internal controls will be mandated by the new Company Law of Japan for all companies with either paid-in capital of at least JPY500 million, or with total indebtedness of at least JPY20 billion.[20] This formalization of internal control requirements under the Company Law is expected to improve the quality of disclosure and financial reporting by Japanese listed companies, in addition to improving compliance programs and risk management systems.

D. Changing Takeover Regulations and Practices

1. *One-year Delay in Implementation of Cash Squeeze-Out Merger Procedure under New Company Law*

Two of the hottest topics in 2005 among listed companies and corporate lawyers were the takeover regulations and takeover defense measures. In February and March of 2005, there was a widely publicized hostile takeover attempt made by Livedoor Co., an Internet portal site operator, to gain control of Nippon Broadcasting System, a radio station operator. This incident was a wakeup call to corporate Japan, and many companies are now seriously considering the adoption of poison pills and other defensive measures; a few companies actually adopted poison pills during the June 2005 shareholder meeting season for the first time in Japanese legal history. Additionally, the effective date of a portion of the new Company Law relating to cash squeeze-out merger procedures and other M&A-related issues has been delayed by one year until May 2007.

2. *Rule on Takeover Defense Measures*

Although unfounded, there was a fear that this portion of the new Company Law might lead to an increase in hostile takeover attempts, and the managements of most listed companies were concerned that they were unprepared for such an alteration to the legal environment, as most companies had never thought seriously about adopting defensive measures. Because in Japan there was no clear rule as to which defensive measures may be permissible and how such measures should be adopted, it was a matter of serious concern for the government that chaos could ensue if M&A activities were to pick up. The Ministry of Economy, Trade, and Industry (METI) took the initiative to form a corporate value study group to announce fair and reasonable rules on takeover defenses and was subsequently joined in this effort by the Ministry of Justice (MOJ). METI and MOJ jointly issued a guideline on permissible takeover defense measures in May 2005.[21] The discussions, how-

20. Art. 2, Item 6; Art. 362, para. 5; Art. 348, para 4; Art 416, para 2 of the Company Law (Law No. 86 of 2005).

21. Ministry of Economy, Trade and Industry, and Ministry of Justice, *Guidelines Regarding Takeover Defense for the Purposes of Protection and Enhancement of Corporate Value and Shareholders' Common Interests* (May 27, 2005), *available at* http://www.midcgroup.com/english/e_libry/index.html (follow hyperlink corresponding to title).

ever, were not yet over, and heated up again over "golden shares" or other special classes of shares (such as those with veto rights or super voting rights) in November 2005. The TSE was forced to find a middle ground to subdue harsh criticism. While the new Company Law allows more flexibility in structuring capital and share schemes, it would be vital that stock exchanges continue to act in the interests of the investing public.

3. *SEL Takeover Rule Reforms*

The Livedoor incident also uncovered a legal loophole in the mandatory takeover rule and led to quick action by the Japanese government to fix the deficiency. However, the Japanese takeover rules under the SEL are apparently not sufficient to create a fair playing field. A working group is due to issue a report on reforms in December 2005, but the report is expected to be a modest one. Again in this area, the SEL changes are expected in 2006, but will perhaps not cover all the necessary issues, leaving some pitfalls.

The TSE rule on takeover defense measures was finalized in March 2006, and the enactment of reforms of takeover regulations under the SEL is expected late in 2006; takeovers, both friendly and hostile, will continue to be a hot issue in 2006.

IV. Developments in the Netherlands

A. Implementation Prospectus Directive

On July 1, 2005, legislation implementing the Prospectus Directive[22] became effective. The relevant amendments to the 1995 Act on the supervision of the securities trade (*Wet toezicht effectenverkeer 1995*, hereinafter Securities Act) provide, among other things, for the introduction of a European passport; with one approved prospectus, securities can be offered in the European Union. The Netherlands Authority for the Financial Markets (AFM) is the competent supervisory authority under the Prospectus Directive in the Netherlands. The former Listing Rules (*Fondsenreglement*) of Euronext Amsterdam were withdrawn and replaced by the Euronext Rule Book (which applies to all Euronext stock exchanges), and the General Rules for the Euronext Amsterdam Stock Market (which apply to Euronext Amsterdam only).

B. Implementation UCITS Directives

On September 1, 2005, legislation implementing the UCITS Directives[23] became effective. The revised Act on the supervision of investment institutions (*Wet toezicht beleggingsinstellingen*) prohibits the offering of participation rights in investment institutions without a license. The revised legislation creates segregated assets (*afgescheiden vermogen*) for investment funds.

Furthermore, most of the recommendations of the Commission on Modernizing Investment Institutions, which was installed in 2004 according to a survey by the AFM of the operation of investment funds in the Netherlands, have been incorporated in the revised Decree on the supervision of investment institutions. The Decree provides for more elaborate provisions with respect to rules laid down in the Act concerning the supervision of

22. Council Directive 71, 2003 O.J. (L354) 64-89.
23. Council Directive 107, 2001 O.J. (L41) 20-34; Council Directive 108, 2001 O.J. (L41) 35-42.

investment institutions and became effective together with the revised Act on the supervision of investment institutions.

C. Implementation Market Abuse Directive

On October 1, 2005, legislation implementing the Market Abuse Directive[24] became effective. The relevant provisions in the Securities Act provide for, among other things, the introduction of a general prohibition against market manipulation. It is prohibited to execute or cause a transaction or trade order in securities that: (i) is likely to give a false or misleading signal as to the supply of, demand for, or price of the securities; or (ii) is an attempt to secure the price of the securities at an artificial level.[25] The Securities Act also requires listed companies, as well as persons who regularly act on behalf of or for the account of such companies, to maintain a list of insiders (i.e., persons who, on a regular or incidental basis, may have access to inside information) and to inform these persons of the market abuse prohibitions and the related maximum sanctions.[26] Furthermore, the General Rules for the Euronext Amsterdam Stock Market were amended.

D. Financial Markets Supervision Act

In the process of the restructuring of the supervision on the financial markets, the third and fourth part of the proposal for the Financial Markets Supervision Act (*Wet financieel toezicht*) was sent to Dutch Parliament. The Financial Markets Supervision Act will replace most of the current financial supervisory legislation. The revised proposal includes the implementation of the Financial Conglomerates Directive.[27] The effective date of the Financial Markets Supervision Act is expected to be January 2007.

E. Financial Services Act

The Financial Services Act (*Wet financiële dienstverlening*) and the Decree on Financial Services were finalized at the end of 2005. The Decree includes more elaborate provisions with respect to rules laid down in the Act, such as expertise and reliability of financial intermediaries, provision of information, and the handling of complaints. The effective date of the Financial Services Act and the Decree is January 2006. The license application form is available on the website of the AFM.[28]

F. Act on the Supervision of Financial Reporting

A proposal for the Act on the supervision of financial reporting (*Wet toezicht financiële verslaggeving*) was sent to Dutch Parliament. The Act is intended to facilitate the transparency and the comparability of financial reporting by listed companies. The Act appoints the AFM as the relevant supervisory authority. As such the AFM shall, among other things,

24. Council Directive 6, 2003 O.J. (L96) 16-25.
25. Section 46 b Dutch Securities Act.
26. Section 47 Dutch Securities Act.
27. Council Directive 87, 2002 O.J. (L275) 32-46.
28. *See* http://www.afm.nl (follow "corporate companies" hyperlink; then follow "information" hyperlink; then follow "forms" hyperlink) (last visited Aug. 26, 2006).

supervise the compliance with the requirement to make financial reports available, as well as compliance with the financial reporting requirement itself. The Act is also intended to facilitate the ability by individual investors to dispute the annual accounts of a listed company.

G. Policy Rule Act on the Supervision of Credit Institutions (Banking Act)

As of January 2, 2005, the amendment to the 2002 Policy Rule regarding the interpretation of certain key terms of the Banking Act and the Exemption Regulation to the Banking Act became effective. The amendment solves, among other things, some practical problems caused by the 2002 Policy Rule. The Policy Rule will be reviewed and amended fundamentally when the Financial Markets Supervision Act becomes effective.

H. Committee Capital Markets

The AFM installed the Committee Capital Markets on April 13, 2005. This Committee advises the board of the AFM on actual matters, new securities legislation, and interpretation of existing regulations regarding public takeover bids, market abuse, and prospectus. The Committee Capital Markets will also advise on the policy regarding financial reporting and accounting firms. This Committee will take over the activities of the former Advisory Committee Listing Rules and the Committee for public takeover bids on securities.

I. Official Market Euronext Amsterdam Renamed Eurolist By Euronext

As of April 4, 2005, the Official Market of Euronext Amsterdam has a new name: Eurolist by Euronext. This name was introduced earlier in Paris, Brussels, and Lisbon and has no direct consequences for the issuers listed on the Official Market. The name change coincides with the integration of Euro.NM Amsterdam and the Official Market. Issuers who do not request transfer from Euro.NM Amsterdam to the Official Market will remain listed on Euro.NM Amsterdam. Euro.NM Amsterdam will continue to exist until the last remaining issuer is delisted.

V. Developments in New Zealand

A. The Securities Legislation Bill

Securities law in New Zealand is poised to undergo major changes with the Securities Legislation Bill, expected to come into force in mid-2006. The bill will significantly change the current law, including a restructure of the insider trading regime, amendments to substantial security holder disclosure, and a brand-new market manipulation regime.

1. *Insider Trading*

The current insider trading regime, under which no one has ever been found liable, has been seen as complex and difficult to enforce. The bill reflects a policy shift from a fiduciary duty to a market integrity focus. The bill extends the scope of insider trading by providing that any person described as an "information insider" who has "material information" that is not "generally available to the market," and who "knows or ought reasonably to know" that the information is inside information, is prohibited from trading. Since the requirement for a link with the company is effectively removed, this is likely to affect a wider group of people. Insider trading will now be subject to criminal sanctions, as opposed to civil sanctions under the Securities Markets Act. The criminal sanctions provide for imprisonment of up to five years and a maximum fine of $300,000 for individuals and $1,000,000 for companies.

2. *Market Manipulation*

The bill also introduces new (for New Zealand) prohibitions on market manipulation and proposes a more general dealing misconduct prohibition with respect to securities. Market manipulation would cover offenses such as the creation of a false impression of trading activity, price movement, or market information. The dealing misconduct prohibitions are similar to those seen in the misleading and deceptive conduct concepts in the Fair Trading Act of 1986 but relate to securities. These prohibitions also carry the criminal sanctions described above.

3. *Substantial Security Holder Disclosure*

The substantial security holder disclosure regime will be changed to only apply to listed voting securities of any particular class. However, contrary to earlier versions of the draft bill, it will not be expanded to include the definition of "relevant interest," a power or control exercised by means of a practice (previously intended to catch equity swaps).

4. *Investment Advisors*

The bill introduces a new investment advisors and brokers disclosure regime, which will replace the current two-tier regime of mandatory disclosure and request disclosure with a regime that is based solely on mandatory disclosure. An investment advisor may not give investment advice, and an investment broker may not receive investment money or property without giving a disclosure statement to the client.

B. Securities Commission Activity

In 2005, the Securities Commission completed 201 enforcement and surveillance matters, including 20 insider trading inquiries. The Commission reached a settlement with Provenco Group Ltd. over insider trading allegations. The Commission considered Provenco to be in possession of inside information about future earnings and business prospects when it made share purchases, including an on-market buy-back of its own shares.

C. Substantial Security Holder Disclosure

The Commission also signaled that it believed the New Zealand substantial security disclosure requirements meant the legislative requirement to disclose as soon as the person knows or ought to know means that any required notice must be filed immediately. This is a significant practical point for institutional shareholders and in takeovers as it is significantly quicker than previous business practice. It is also faster than the general Australian requirement of filing within two business days.

D. Overseas Investment Act

The new Overseas Investment Act came into force on August 25, 2005. The Act dissolves the Overseas Investment Commission and establishes the Overseas Investment Office, a specialist body within Land Information New Zealand. An important change is the raising of the threshold for non-land business asset investment (or where a 25 percent or greater shareholding is to be acquired) from $50 million to $100,000 million.

This new Act retains screening over all sensitive land. Land will be classified as sensitive land if it exceeds the area threshold and comprises or adjoins a certain type of land such as a lakefront or historic area. Screening is not retained on land adjoining some non-sensitive reserves, for example drainage and hospital reserves.

E. Takeovers

The Takeovers Panel had a busy year in 2005, heading to the High Court for the first time over the partial takeover offer by Delegat's Wines Estate Ltd. for 50.1 percent of the shares of Oyster Bay Marlborough Vineyards Ltd. The High Court upheld the Panel's decision that certain information was material and should have been disclosed in the target company statement. The exact remedy to be given by the High Court awaits a further High Court hearing.

VI. Developments in South Korea

A. Securities Class Action Act Takes Effect

The Securities Class Action Act (SCAA), which became effective on January 1, 2005, is designed to provide remedies for small investors and minority shareholders of publicly listed companies in Korea and to improve corporate governance. The SCAA takes effect in two different stages, and the scope of actions that can be brought under the SCAA is limited to claims for damages caused by (i) false disclosure made in a registration statement or annual/periodic report, (ii) insider trading, (iii) share price manipulation, or (iv) inadequate audit. Initially, the scope of companies is limited to publicly listed companies in Korea with assets of at least KRW 2 trillion (approximately US $2 billion). From January 1, 2007, the scope of companies will be expanded to cover all publicly listed companies in Korea.

After the SCAA became effective, the Korean government enacted a special amendment to the SCAA, effective March 2, 2005, to provide support to publicly listed companies (with assets of at least KRW 2 trillion) that may be targets of securities class action lawsuits. Such special amendment provides for a grace period in which publicly listed companies can make accounting adjustments to correct past window dressing on their financial statements published through December 31, 2006, although such corrections may not serve as the basis for a securities class action lawsuit. To date, no securities class action lawsuit has been filed under the SCAA.

B. Korea Joins the International Sale of Goods Convention

Korea joined the UN Convention on Contracts for the International Sale of Goods of 1980 (CISG) as the sixty-third member, effective as of March 1, 2005. The current signatories to the CISG include, among others, the United States, Germany, France, China, and Canada. The CISG is composed of 101 articles that provide rules regulating the international sale of goods in such matters as formation of contract, obligations of the parties, remedies for breach of contract, and risk of loss. The CISG also ensures flexibility by allowing parties to exclude by agreement any provisions of the CISG. Unless the parties to a contract agree to opt out, CISG provisions will govern a contract for a sale of goods between parties located in different member countries.

C. Amendments to the Securities and Exchange Act

The Korean government amended the Securities and Exchange Act (SEA) to provide the management of a publicly traded company in Korea with time to defend against hostile takeovers. These amendments, which became effective on March 29, 2005, require an investor with 5 percent or more equity shareholding in a public company to specify the purpose of share acquisition as either for pure portfolio investment or as investment for influencing management. In case the purpose of share acquisition is for influencing management, it also imposes a cooling-off period. The amendments also lift certain restrictions regarding tender offers that now allow an investor to make multiple tender offers within a six-month period and allow a target company to issue voting shares and other equity-linked debt securities during the tender offer period.

By way of background, under the SEA, an investor (whether Korean or foreign) who has, individually or jointly with specially related persons, come to own or hold 5 percent or more of the total voting shares or other securities equivalent to voting shares of a public company must file a substantial shareholding report (5 percent Report) with the Korean Financial Supervisory Commission (FSC) and the Korea Exchange (KRX) within five days (excluding Sundays and holidays) after such threshold has been met. Subsequently, if there is a change in either the investor's shareholding by at least 1 percent (upward or downward) or a change in the purpose for shareholding, such change also should be reported within five days.

As of March 18, 2005, the FSC instituted a new 5 percent Report form, which must be used for any 5 percent Report filed on or after March 29, 2005. With respect to shareholding for pure portfolio investment purposes, the new 5 percent Report form streamlined the relevant reporting requirement to exclude details regarding purpose and the source of funds or assets. On the other hand, with respect to shareholding for purposes of influencing management, the new 5 percent Report form requires more detailed information on such purpose and the source of funds or assets. Generally, an investor is deemed to be influencing the management of a public company if it seeks to, among others things, appoint, dismiss, or suspend a director or auditor of that public company or change that public company's articles of incorporation regarding directors, boards of directors, or other bodies. Under the SEA, an investor who reports the purpose of shareholding as influencing the management of a public company is prohibited from acquiring additional voting shares in that public company and from excercising voting rights of all voting shares held in that public company for five days after filing such report.

D. Amendments to the Real Estate Investment Trust Act

The Korean government amended the Real Estate Investment Trusts (REIT) Act in order to facilitate the use of real estate investment trusts (i.e., companies that raise funds from investors by issuing shares, and invest such funds in real estate) by relaxing regulations on their establishment and business activities. The amendments, which became effective on April 1, 2005, provide for the diversification of the forms of such trusts and the promotion of the establishment and use of them. Such amendments include the following:

(i) The minimum capital requirement has been reduced from KRW 50 billion to KRW 25 billion (approximately US $25 million). In addition, in-kind contribution (i.e., contribution of real estate) to the capital of such trusts will be allowed within the limit of 50 percent of the capital.

(ii) Real estate investment trusts are allowed to engage in real estate development business upon resolution at a shareholders' meeting, instead of obtaining approval from the Korean Ministry of Construction and Transportation. In addition, the maximum limit on the amount of capital to be invested in such business by such trusts has been increased from 30 percent of its total capital to 30 percent of its assets.

E. Enactment of the Employee Retirement Income Security Act

The Korean government enacted the Employee Retirement Income Security Act (ERISA), which took effect on December 1, 2005, to contribute to the welfare of employees after retirement by providing alternatives to the existing lump sum severance payment system. The ERISA provides for two basic types of retirement pension systems for employees: (i) a defined contribution plan; and (ii) a defined benefit plan. Under the ERISA, with the consent of relevant employees or their appropriate employee representative, an employer may select among the existing lump sum severance payment plan, the defined contribution plan and the defined benefit plan for each employee. An employer planning to establish a retirement pension system must prepare retirement pension rules in consultation with relevant employees or their appropriate employee representative and retain a registered retirement pension system operator (typically a financial institution) to manage and administer the selected retirement pension plan.

F. Preparation of the Bill on Regulating Foreign Legal Consultants

On August 30, 2005, the Korean Minister of Justice established a special subcommittee (Subcommittee) for the preparation and drafting of the Foreign Legal Consultants Act, which will for the first time officially manage and supervise foreign-licensed attorneys practicing in Korea (Foreign Legal Consultants). The Subcommittee, which is made up of ten members from the business and legal communities, academia, and government, was established to prepare for the liberalization of the Korean legal services market, which is one of the last legal services markets in Asia still closed to foreign law firms and, to a certain extent, foreign-licensed attorneys. The Subcommittee is to draft a bill regulating Foreign Legal Consultants, which will set forth for the first time in Korea the qualification requirements for Foreign Legal Consultants and the scope of legal practice and supervision of Foreign Legal Consultants. In April 2006, the Subcommittee announced the initial draft of the bill, which appears to mirror similar regulations in other developed countries. The bill is expected to be passed by the Korean National Assembly at the end of 2006, and to become effective in 2007.

The Korean government has submitted a plan for liberalization of its legal services market in the Doha Development Agenda negotiations that are in progress in the World Trade Organization. Since such negotiations are expected to be completed by the end of 2006, the bill is to lay the groundwork for implementing the anticipated agreement from such negotiations for the liberalization of the Korean legal services market. Such agreement includes the following:

(i) Foreign Legal Consultants will be permitted to provide legal advice on the laws of the jurisdiction where they are licensed and on international public law.
(ii) Foreign law firms will be permitted to establish offices in Korea.
(iii) Foreign Legal Consultants will not be permitted to form partnerships with, or employ, Korean-licensed attorneys.

VII. Developments in Turkey

A. Turkish Capital Markets Board Regulatory Activity

The Law on Capital Markets No. 2499[29] (Capital Markets Law) is the primary legislation regulating capital markets in Turkey. The Turkish Capital Markets Board (CMB) is the independent government authority regulating and monitoring capital market activities through issuance of regulations and communiqués in line with the Capital Markets Law.

Through late 2004 and into 2005, the CMB promulgated a number of regulatory acts with the aim of providing a better investment environment and ensuring compliance with the acquis communautaire[30] in line with the Ministry of Council's decision dated June 24, 2003 for the coordination of the adoption of the European Community legislation. However, progress in 2005 was more limited than that achieved the previous year. The most important change was the dematerialization of certain capital market instruments.

Pursuant to the Central Registry Agency Regulation,[31] the Central Registry Agency (*Merkezi Kayıt Kuruluşu A.Ş.*) was established for, and authorized to, among other things: monitor dematerialized (i.e., non-printed) capital market instruments and rights pertaining thereto in electronic form on an issuer, broker, and rights-holder basis; monitor and ensure the cross-accuracy of the records between issuers, brokers, and rights-holders; request corrections; ensure privacy of the records; carry out dematerialization procedures; operate and represent the Investors Protection Fund; and carry out the external liquidation process for brokers as determined by the CMB.

As per the CMB's decision numbered 43/1318 and dated October 28, 2005,[32] the dematerialization of all stocks currently trading on the Istanbul Stock Exchange (ISE) was realized as of November 28, 2005.[33] Except for minor adjustments, the mechanism currently employed for clearing and settlement will not be altered and will continue to be administered by Takasbank,[34] whereas the custody function will be carried out by the Central Registry Agency alone. The most important changes to the custody system are summarized below:

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29. Capital Markets Board of Turkey, Law No. 2499: Capital Market Law (2002), *available at* http://www.cmb.gov.tr/regulations/files/CMB_law.pdf.

30. The entire body of the laws of the EU is known as *acquis communautaire*. This includes all the treaties, regulations and directives passed by the European institutions as well as judgments. *See* European Commission, *Development: Legislation* (June 23, 2004), http://europa.eu.int/comm/development/body/legislation/index_en.htm.

31. Capital Markets Board of Turkey, Regulation on Principles and Procedures of Progressive Liquidation of Intermediary Institutions (Official Gazette No: 24439) (June 21, 2001) (on file with author).

32. *See* CMB Bulletin No. 2005/45 for the period between October 24—28, 2005 (on file with author.)

33. Similarly, as per its decision numbered 24/777 and dated June 16, 2005, the CMB decided to commence the necessary steps to dematerialize mutual fund participation certificates (*yatırım fonu katılma belgeleri*) as well.

34. *Takasbank* is the acronym for Istanbul Stock Exchange Settlement and Custody Bank (*İstanbul Menkul Kıymetler Borsası Takas ve Saklama Bankası A.Ş.*,) which is the clearing and settlement center for the Istanbul Stock Exchange and the central securities depository of Turkey.

(i) Dematerialized stocks will no longer be represented by physical share certificates and custody of the dematerialized stocks is transferred from *Takasbank* to the Central Registry Agency.

(ii) Upon expiration of a one-year transition period, all different kinds of dematerialized stocks will be abolished by amending the articles of association of the relevant listed companies.

(iii) In order to be valid vis à vis third parties, any transfer, disposal of, or encumbrance (establishment of pledges and usufruct rights) on dematerialized stocks needs to be registered with the Central Registry Agency in the order of the notification date.

B. Other Relevant Developments

Turkey is currently undergoing a rapid and drastic transformation into a modern, secular, and democratic nation with a strong market economy in order to become a full member of the European Union (EU). The ongoing transformation was confirmed by the EU's decision to open accession talks with Turkey on October 3, 2005.[35] As a result of this continuing reform process, certain major bills are currently pending enactment. In order to develop a full-fledged mortgage banking system comparable to European standards, the CMB prepared a revised Draft Law Related To The Housing Finance System in Turkey[36] proposing amendments to various pieces of legislation. In August 2005, the CMB made available to the public its draft of the proposed amendments to the Capital Markets Law for the purposes of integration with the EU legislation.[37] The following summarizes some of the most important amendments introduced by the draft:

(i) *Publicly Listed Companies*: Mergers and spin-offs (partial division or split-off) in publicly held companies will be governed in compliance with the EU legislation. Furthermore, under the authorized share capital system, the authority of the board of directors to increase the capital of public companies will be limited to a maximum of five years. In the case of special events, the scope of mandatory public disclosures will be extended to increase transparency of listed companies and the level of information available to investors. Those that do not comply with the mandatory tender offer requirements will have their voting rights suspended by

35. The basis for the accession negotiations are laid down in a document called *Negotiation Framework* dated October 3, 2005 (*See* http://europa.eu.int/comm/enlargement/docs/pdf/st20002_en05_TR_framedoc.pdf.) On October 3 2005, the negotiations were symbolically launched, and on October 20, 2005, the screening was opened for some of the 35 chapter headings. Screening is the formal process of examination of the entire body of laws of the EU by the Commission in order to identify for, and explain to, the Turkish authorities the legal framework and administrative capacities that need to be adapted so as to apply EU law as a Member State. The screening will be conducted in two stages. During the first stage, the Commission would explain its *acquis* to Turkey, while in the second stage, Turkey would explain its laws. The screening process is scheduled to take about a year to complete and will be followed by negotiations between the Commission and Turkey on a chapter-by-chapter basis.

36. *See* Capital Markets Board of Turkey, *The Draft Law Amending The Laws Related to Housing Finance System*, *available at* www.cmb.gov.tr/housingfinance/mortgage_cmb_draft_law.pdf (last visited July 7, 2006) (unofficial translation from Turkish into English on file with author).

37. *See* http://www.spk.gov.tr/HaberDuyuru/duyurular/SPKn/SPKn_tasarisi_taslagi.pdf (in Turkish, on file with author).

court decisions. Moreover, non-compliant shareholders may be fined with a penalty that is proportional to the amount of investment not incurred as a result of the omitted mandatory tender offer. Currently, persons who acquire 25 percent of the voting stock of public companies are compelled to launch a mandatory tender offer for the remaining shares outstanding, and holdouts may be fined with a penalty. The draft will also grant the CMB authority to regulate the purchase of treasury shares, which is currently prohibited under both the Turkish Commercial Code and the capital markets legislation.

(ii) *Pooled Investment Vehicles*: The draft will further the development of the mortgage-based housing finance model introduced by the recent draft law on mortgage banking expected to be enacted soon. The restrictions imposed on the incorporators of mutual funds (*yatırım fonu*) will be abolished and the conditions for incorporation of investment trusts (*yatırım ortaklıkları*) will be simplified. The principles for mutual fund managers and management will be re-regulated. The principles for valuation of capital in kind, invested in real estate investment trusts will be re-determined. Portfolio custody principles will be set out, and the restrictions regarding securities that are traded by mutual funds will be abolished.

(iii) *Widening the Scope of Investors' Protection*: All financial instruments will become subject to the Investors' Protection Fund, and the upper limit of the secured amount per individual investor is increased to the YTL equivalent of €20,000.

(iv) *Increasing Effectiveness of Penalties and Measures*: Measures for insider-trading activities will be harmonized with EU legislation. Public prosecutors will only be allowed to examine defendants and witnesses in the presence of supervisors from the CMB. Those who engage in capital markets activities without obtaining the required permits will be subjected to bankruptcy proceedings. Furthermore, monetary penalties will be applicable to financial crimes. The CMB will be granted the authority to request from the courts the deposition of directors who violate the relevant laws and regulations and will be entitled to request appointment of new directors from the courts. The CMB will further be granted the authority to fine those who fail to fulfill the public disclosure requirements imposed by the Capital Markets Law. Finally, new penalties will be incorporated with respect to joint stock corporations that proceed with public offerings without fulfilling the registration requirement of the CMB.

The overhaul of the Capital Markets Law coincides with certain amendments to the existing tax regime. The tax system will be simplified, with special focus on the taxation of foreign corporate investors. Government bonds that used to have tax advantages over corporate bonds will become subject to the same taxation principles as corporate bonds. Since convertible bonds have not been issued by Turkish companies for the last ten years, and the tax regime in 2006 is expected to level the playing field for corporate and government bonds, this may be considered method for increasing corporate bond issuing transactions.

VIII. Developments in the United States

A. SEC Securities Offering Reform

On November 3, 2004, the Securities and Exchange Commission (SEC) issued proposed rule changes under the Securities Act of 1933, as amended (Securities Act) and the Exchange

Act of 1934, as amended (Exchange Act) to modernize the securities offering and communication requirements specified therein.[38] The final rules were published on July 19, 2005, and became effective on December 1, 2005.[39] Foreign private issuers and domestic issuers are treated similarly under the rules.

1. *New Category of Issuer*

The rules establish a new category of issuer, a "well-known seasoned issuer" (WKSI), for certain large issuers that are followed by sophisticated investors, analysts, and the financial press. The WKSI category is intended to supplement the existing categories of issuers, which include seasoned issuers, unseasoned Exchange Act reporting issuers, and non-reporting issuers. The SEC's rationale behind the WKSI category is to recognize that large, well-known issuers tend to have a more regular dialogue with (and are subject to greater scrutiny by) investors and market participants through the press and other media.

The SEC defines a WKSI as an issuer that is required to file reports pursuant to Section 13(a) or Section 15(d) of the Exchange Act and satisfies the following:

(i) is not an ineligible issuer (this includes penny stock companies, blank-check companies, shell companies, and issuers who have violated the securities laws or who have experienced financial difficulties) and is not making an ineligible offering;
(ii) is current in its reporting obligations under the Exchange Act and timely in satisfying those obligations for the preceding twelve months;
(iii) is eligible to register a primary offering of its securities on Form S-3 or Form F-3; and
(iv) either (a) has outstanding a minimum worldwide $700 million of common equity market capitalization held by non-affiliates (i.e., "public float") within sixty days of its eligibility determination date, or (b) has issued at least $1 billion aggregate amount of non-convertible debt securities in registered offerings for cash during the past three years and registers only debt securities within sixty days of its eligibility determination date.

2. *Liberalization of Communications Related to Registered Offerings*

In the new rules, the SEC relaxes some of the "gun-jumping" restrictions related to communications, procedures, and delivery of information in varying degrees, based upon the reporting status of the issuer. For all reporting issuers, regularly released factual business and forward looking information will now not be deemed to be an offer, provided that such release is in the issuer's ordinary course of business and consistent with past practice. For non-reporting issuers, factual business information (but not forward looking information) that is regularly released to persons other than in their capacity as investors will not be deemed to be an offer. The widest latitude is granted to WKSIs, for whom oral and written communications, including the use of a free-writing prospectus, will not be deemed to be an offer, but in many cases will require filing with the SEC. Communications occurring more than 30 days before an offering will not be deemed to be an offer, as long as there is no reference to the offering; this restriction does not apply to WKSIs.

38. Securities Offering Reform, Securities Act Release Nos. 33-8501, 34-50624 and IC-26649 (Nov. 3, 2004).

39. Securities Offering Reform, Securities Act Release Nos. 33-8591, 34-52056, IC-26993 and FR-75 (July 19, 2005).

3. *Free-Writing Prospectus*

The rules also permit the use of a free-writing prospectus by WKSIs prior to effectiveness of a registration statement and by others after a registration statement has been filed. A free-writing prospectus includes any written or electronic communication outside the statutory prospectus that is made by an issuer or other offering participant, and either refers to the offer or would constitute an offer that would be subject to liability under Section 12(a)(2). Only WKSIs are able to use free-writing prospectuses prior to the filing of a registration statement; non-reporting issuers and non-WKSIs are able to use a free-writing prospectus only upon the filing of a registration statement. In addition, the statutory prospectus must precede or accompany any free-writing prospectus of a non-reporting issuer or non-WKSI. Electronic road shows are considered free-writing prospectuses, and therefore must be filed, unless a copy of the electronic road show is posted on the issuer's website and is readily available to the public. Similarly, media interviews are also free-writing prospectuses and, if they involve issuers or underwriters, must be filed with the SEC.

Any free-writing prospectus used by any person is subject to liability under Section 12(a)(2) of the Securities Act and to the antifraud provisions of the securities laws. Because such a prospectus is not deemed to be part of the registration statement, however, it is not subject to liability under Section 11 of the Securities Act.

4. *Registrations and Shelf Offerings*

The new rules liberalize the shelf registration process for WKSIs by permitting their shelf registrations to become effective automatically, and to register various classes of securities, without allocation or distinction between primary and secondary shares. Furthermore, WKSIs are permitted to pay in advance or to use a pay-as-you-go process for payment of registration fees.

Under the rules, prospectus supplements are deemed part of the registration statement for all shelf offerings. The rules essentially codify the information that may be omitted from a base prospectus in a shelf offering and included in subsequently filed prospectus supplements, thereby providing more direction for shelf offering participants. The new rules eliminate the limitation under Rule 415 permitting registration only of the number of shares intended to be sold within two years, instead requiring that the shelf be updated with a new registration statement every three years. The rules also permit immediate shelf takedowns and allow material changes to the plan of distribution described in the prospectus to be made by filing a prospectus supplement.

5. *Research Reports, Rule 134 "Tombstone Ads" and Prospectus Delivery*

The SEC has also substantially expanded the existing safe harbors available to broker-dealers for research reports, including the types of issuers covered and the conditions to publication or dissemination. The SEC expanded Rule 134 to allow offering participants to communicate a broader range of routine information about the offering, issuer, and procedural matters; however, even with this reform, Rule 134 is not permitted to test investor interest in a proposed offering (i.e., testing the waters). There will be no mandated method of prospectus delivery; the SEC filing is deemed to constitute availability for investor consultation, as access equals delivery. Issuers must, however, notify investors that they have purchased securities in a registered transaction.

6. *Revised Required Disclosure In Exchange Act Reports*

The SEC now requires additional disclosure in three areas: (i) risk factors; (ii) unresolved SEC staff comments; and (iii) disclosure of status as a voluntary filer under the Exchange Act. First, the SEC has extended risk factor disclosure to annual reports and registration statements and requires quarterly updates to reflect any material changes with regard to risk factors. The scope of risk factor disclosure under the Exchange Act is the same type of disclosure as in a Securities Act registration statement, namely, the most significant risks facing an issuer.

Also, the SEC now requires all accelerated filers to disclose in their annual reports written SEC comments that were issued more than 180 days before the end of the fiscal year covered by the annual report and which remain unresolved as of the date of the filing of the annual report, and that the issuer believes to be material. This must be sufficient to disclose the substance of the comments, and issuers can include in such disclosure their position resolving any such unresolved comments.

In addition, an issuer must disclose its status as a voluntary filer of Exchange Act reports in order to inform investors and other market participants that an issuer is a voluntary filer (and may cease to file its Exchange Act reports at any time). This will also enable the SEC to identify voluntary filers more easily in order to monitor such issuers' use of proposed communications rules and other regulatory requirements.

B. Sarbanes-Oxley Section 404 Compliance Date Extensions

On March 2, 2005, and again on September 22, 2005, the SEC extended the dates for foreign private issuers to comply with amendments to its rules under the Exchange Act that were made in 2003 pursuant to Section 404 of the Sarbanes-Oxley Act of 2002.[40] The amendments require SEC-reporting companies to include in their annual reports a report of management on the company's internal control over financial reporting, and to evaluate, as of the end of each fiscal period, any change in the company's internal control over financial reporting that occurred during the period that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting.

As a result of the extension granted, a foreign private issuer that is an accelerated filer (as defined in Rule 12b-2 under the Exchange Act) and that files its annual reports on Form 20-F or 40-F must begin to comply with the internal control over financial reporting requirements for its first fiscal year ending on or after July 15, 2006—a one-year extension from the previously established July 15, 2005 compliance date. Foreign private issuers that are not accelerated filers must begin to comply with the requirements for their first fiscal year ending on or after July 15, 2007. The SEC similarly has extended the compliance date for these companies relating to requirements regarding evaluation of internal control over financial reporting and management certification requirements.

40. Management's Report on Internal Control over Financial Reporting and Certification of Disclosure in Exchange Act Periodic Reports of Non-Accelerated Filers and Foreign Private Issuers, Exchange Act Release Nos. 33-8545 and 34-51293 (Mar. 2, 2005); Management's Report on Internal Control Over Financial Reporting and Certification of Disclosure in Exchange Act Periodic Reports of Companies that Are Not Accelerated Filers, Securities Exchange Act Release Nos. 33-8618 and 34-52492 (Sept. 22, 2005).

C. SEC Accommodation for International Financial Reporting Standards

On April 12, 2005, the SEC published amendments to Form 20-F providing a one-time accommodation relating to financial statements prepared under International Financial Reporting Standards (IFRS) for foreign private issuers registered with the SEC.[41] This accommodation applies to foreign private issuers that adopt IFRS prior to or for the first financial year starting on or after January 1, 2007.

Foreign private issuers that have ongoing SEC reporting requirements are generally required to present, in their annual reports and registration statements filed with the SEC, audited statements of income, changes in shareholders' equity, and cash flows for each of the past three financial years, prepared on a consistent basis of accounting.

At the beginning of 2003, the International Accounting Standards Board had not finalized some of the IFRS that many foreign private issuers will be required to apply retrospectively when they adopt IFRS for the first time for year 2005. Consequently, for foreign issuers switching to IFRS, compliance with SEC requirements would have been difficult because these issuers would have been forced to implement accounting standards that were not yet finalized during the reporting period to which they must be applied.

The accommodation permits eligible foreign private issuers, for their first year of reporting under IFRS, to file two years rather than three years of statements of income, changes in shareholders' equity, and cash flows prepared in accordance with IFRS, with appropriate related disclosure. The accommodation retains current requirements regarding the reconciliation of financial statement items to generally accepted accounting principles as used in the United States.

41. First-Time Application of International Financial Reporting Standards, Securities Exchange Act Release Nos. 33-8567, 34-51535 and IS-1285 (Apr. 12, 2005).